

REPORT OF EXAMINATION
OF THE
REPUBLIC INDEMNITY COMPANY OF AMERICA
AS OF
DECEMBER 31, 2008

Participating State
and Zone:

California

Filed January 21, 2010

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Los Angeles, California
November 13, 2009

Honorable Alfred W. Gross
Chairman of the NAIC Financial
Condition Subcommittee
Commissioner of Insurance
Virginia Bureau of Insurance
Richmond, Virginia

Honorable Morris Chavez
Secretary, Zone IV-Western
Superintendent of Insurance
New Mexico Insurance Division
Santa Fe, New Mexico

Honorable Steve Poizner
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Chairman, Secretary, and Commissioner:

Pursuant to your instructions, an examination was made of the

REPUBLIC INDEMNITY COMPANY OF AMERICA

(hereinafter also referred to as the Company) at its home office located at 15821 Ventura Boulevard, Encino, California 91436.

SCOPE OF EXAMINATION

The previous examination of the Company was made as of December 31, 2004. This examination covers the period from January 1, 2005 through December 31, 2008. The examination was conducted pursuant to the National Association of Insurance Commissioners' plan of examination. The examination included a review of the Company's practices and procedures, an examination of management records, tests and analyses of detailed transactions within the examination period, and an evaluation of the assets and a determination of liabilities as of December 31, 2008, as deemed necessary under the circumstances.

The examination was conducted concurrently with the examination of the Company's subsidiary, Republic Indemnity Company of California.

In addition to those items specifically commented upon in this report, other phases of the Company's operations were reviewed including the following areas that require no further comment: corporate records; fidelity bonds and other insurance; officers', employees' and agents' welfare and pension plans; growth of company; business in force by states; loss experience; and sales and advertising.

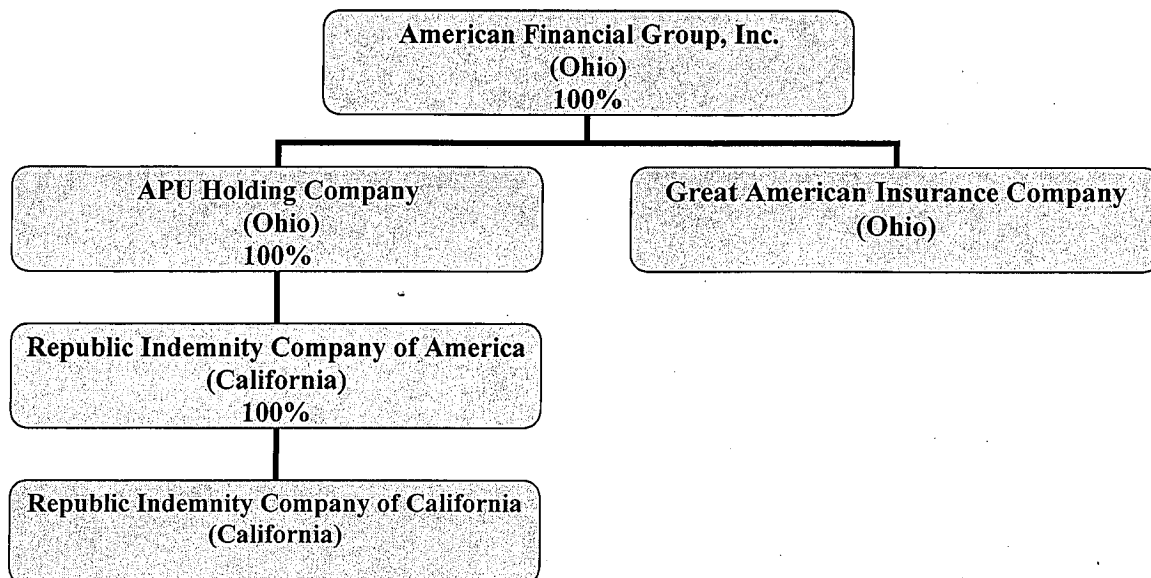
COMPANY HISTORY

During the four-year period under review, the Company received gross paid-in and contributed surplus in the form of cash and securities totaling \$69,666,852. The contributions were provided by the Company's parent, APU Holding Company. As a result of the contributions, the balance of the gross paid-in and contributed surplus increased from \$109,431,116 to \$179,097,968 during the intervening period.

With respect to the four-year period under review, dividend distributions to the Company's sole stockholder totaled \$291,600,000. Prior approval for a \$50,000,000 extraordinary dividend distribution (2005) was granted by the California Department of Insurance.

MANAGEMENT AND CONTROL

Ultimate control of the Company is maintained by American Financial Group, Inc. The following abbreviated organizational chart depicts the Company's relationship within the holding company system:



Management of the Company is vested in a nine-member board of directors elected annually. A listing of the members of the board and principal officers serving as of December 31, 2008 follows:

Directors

| <u>Name and Residence</u> | <u>Principal Business Affiliation</u> |
|---|--|
| Gary J. Gruber Cincinnati, Ohio | Senior Vice President Great American Insurance Company |
| David Harkins Westlake Village, California | Senior Vice President - Underwriting Republic Indemnity Company of America |
| Karen Holley Horrell Cincinnati, Ohio | Senior Vice President Great American Insurance Company |
| Keith A. Jensen Cincinnati, Ohio | Executive Vice President Great American Insurance Company |
| Donald D. Larson Cincinnati, Ohio | Executive Vice President Great American Insurance Company |
| Dwayne T. Marioni Novato, California | President and Chief Executive Officer Republic Indemnity Company of America |

Name and ResidencePrincipal Business Affiliation

David P. Mitchell
Agoura Hills, California

Senior Vice President – Claims
Republic Indemnity Company of America

Dion G. Riley
Chatsworth, California

Senior Vice President , Chief Financial
Officer and Treasurer
Republic Indemnity Company of America

David J. Witzgall
Villa Hills, Kentucky

Senior Vice President
Great American Insurance Company

Principal OfficersNameTitle

Gary J. Gruber
Dwayne T. Marioni
Dion G. Riley

Chairman
President and Chief Executive Officer
Senior Vice President, Chief Financial
Officer, and Treasurer

Melinda A. Kreger
Frank M. Ceraolo
David Harkins
Steven A. Gallacher
David P. Mitchell

Vice President and Secretary
Senior Vice President
Senior Vice President
Senior Vice President
Senior Vice President

Management Agreements

Investment Services Agreement: The Company is party to an Investment Services Agreement with American Money Management Corporation (AMMC), an affiliated entity, as amended as of January 1, 1996. Under the terms of the agreement, AMMC provides management and accounting services related to the Company's investment portfolio. Expenses incurred by AMMC for services under this agreement are to be charged and paid quarterly and pro-rated on the basis of the proportion of the Company's portfolio value to the total portfolio value administered by AMMC. During the years 2005, 2006, 2007, and 2008, the Company paid AMMC \$269,561, \$300,300, \$444,048, and \$318,875, respectively.

Claims Services Agreement: Effective August 30, 2006, the Company and its subsidiary, Republic Indemnity Company of California (RICC), entered into a Claims Service Agreement with Great American Insurance Company (GAI), an affiliate. Under the terms of the agreement, GAI provides services consisting of investigation, handling and adjustment of claims arising out of incidental workers' compensation insurance policies issued by GAI at the request of the Company covering risks in states where the Company is not licensed. All premiums related to such policies are ceded to the Company. The agreement stipulates that the Company is obligated to pay GAI fees equal to the sum of costs and expenses incurred by GAI in providing the services. Since the inception of the agreement through year-end 2008, GAI has been paid a combined total of \$89,401 for services provided to the Company and its wholly-owned subsidiary.

Authorization to implement the aforementioned agreement was granted by the California Department of Insurance (CDI) via a letter dated August 14, 2007. In the authorization for use letter, the CDI reminded the Company that agreements should not be executed in advance of the CDI's authorization under California Insurance Code (CIC) Section 1215.5(b)(4). The Company is hereby reminded that it must observe the requirements stipulated in CIC Section 1215.5(b)(4).

Tax Allocation Agreement: Effective December 31, 2005, a tax allocation agreement was implemented between American Financial Group, Inc. (AFG) and certain specified subsidiaries including the Company. This agreement supersedes the previous tax allocation agreement which had been in effect since 1974. Under the terms of the agreement, federal income tax returns are filed on a consolidated basis on behalf of AFG and the specified subsidiaries. The Company's tax liability or refund is determined as if the Company was filing on a separate basis. Approval of the new tax allocation agreement was granted by the CDI on November 29, 2005.

General Service Agreement: Effective January 1, 1996, the Company and RICC have been subject to a General Services Agreement by and between 49 affiliated insurance companies (collectively referred to as the Parties) of the GAIC holding group. Under the terms of the agreement, the Parties furnish various services such as printing, office duplicating, telecommunications, purchasing,

personnel, administrative and data processing to each other. Charges for these services are based on actual cost. During the years 2005, 2006, 2007, and 2008, the Company was charged \$3,821,156, \$3,450,592, \$3,205,823, and \$4,095,918, respectively.

TERRITORY AND PLAN OF OPERATION

As of December 31, 2008, the Company was licensed to write various property and casualty coverages in the District of Columbia and the following 38 states:

| | | | |
|------------|-------------|----------------|----------------|
| Alabama | Illinois | Missouri | South Carolina |
| Alaska | Indiana | Montana | South Dakota |
| Arizona | Iowa | Nebraska | Tennessee |
| Arkansas | Kansas | Nevada | Texas |
| California | Kentucky | New Mexico | Utah |
| Colorado | Louisiana | North Carolina | Washington |
| Delaware | Maine | Ohio | West Virginia |
| Georgia | Maryland | Oklahoma | Wisconsin |
| Hawaii | Michigan | Oregon | |
| Idaho | Mississippi | Rhode Island | |

During 2008, the Company wrote \$116.6 million of direct premiums; 80% pertained to workers' compensation business, the remainder consisted of excess liability workers' compensation coverages. Effective July 1, 2007, the Company began writing excess workers' compensation coverages which is categorized in the annual statement as "other liability." Of the total direct premiums written, \$72.7 million (62.3%) was written in California. The collective direct premiums written in Alaska, Arizona and Nevada represented approximately 23.7% of the total and, the remaining 14% was written in various states.

Workers' compensation business is written through 1,150 independent agents who target all risk classes except petroleum and mining. In recent years, the Company has focused on skilled classes and small "Main Street" retail operations, deemphasizing construction and other higher risk classes. The Company maintains branch offices in Englewood, Colorado; Henderson, Nevada; Phoenix, Arizona; Portland, Oregon; Richardson, Texas; and Encino, San Diego and San Francisco, California.

REINSURANCE

Intercompany Pooling Agreement

The Company and its wholly-owned subsidiary, Republic Indemnity Company of California (RICC), are parties to an intercompany pooling agreement. Under the terms of the agreement, substantially all direct and assumed business written by the two companies is pooled. Premiums, losses, and expenses incurred are then reapportioned and shared by the Company and RICC in the proportions of 97% and 3%, respectively.

Assumed

The Company has two fronting arrangements with Great American Insurance Company (GAIC), an affiliate, covering (1) out of state incidental workers' compensation and (2) excess liability workers' compensation risks; 100% of the business written by GAIC is ceded to the Company.

Ceded

The following is a summary of the Company's principal reinsurance agreements in-force as of December 31, 2008:

| Type of Contract | Reinsurer's Name | Company's Retention | Reinsurer's Maximum Limits |
|---|--|---------------------|---|
| <u>Workers' Compensation</u> <u>XOL:</u> | | | |
| 1 st Excess of Loss | Swiss Reinsurance America Corporation - Authorized Reinsurer (50%) Republic Indemnity Group (50%) | \$1 million | \$1 million (As a result of the Group's 50% participation interest in the agreement, the reinsurer's maximum liability is limited to 50% of \$1 million or \$500,000) |

| Type of Contract | Reinsurer's Name | Company's Retention | Reinsurer's Maximum Limits |
|---|--|---------------------|---|
| 2 nd Excess of Loss | Swiss Reinsurance America Corporation – Authorized Reinsurer (60%) Republic Indemnity Group (40%) | \$2 million | \$3 million (As a result of the Group's 40% participation interest in the agreement, the reinsurer's maximum liability is limited to 60% of \$3 million or \$1.8 million) |
| 3 rd Excess of Loss | Swiss Reinsurance America Corporation – Authorized Reinsurer (85%) Lloyds Syndicate #1084 – Authorized Reinsurer (5%) Catlin Underwriting – Authorized Reinsurer (5%) Hannover Ruckversicherungs Aktiengesellschaft – Authorized Reinsurer (5%) | \$5 million | \$5 million |
| <u>Workers' Compensation Catastrophe XOL:</u> | | | |
| 1 st Excess of Loss | Lloyds Syndicate #2987 – Authorized Reinsurer (20%) Aspen Insurance UK Ltd – Authorized Reinsurer (20%) Various Authorized and Unauthorized Reinsurers (60%) | \$10 million | \$10 million |
| 2 nd Excess of Loss | Partner Reinsurance Company of the US – Authorized Reinsurer (10%) Munich Reinsurance – Authorized Reinsurer (10%) Various Authorized and Unauthorized Reinsurers (80%) | \$20 million | \$30 million |
| 3 rd Excess of Loss | Munich Reinsurance – Authorized Reinsurer (25%) Various Authorized and Unauthorized Reinsurers (75%) | \$50 million | \$50 million |
| 4 th Excess of Loss | Imagine Underwriting APS on behalf of Lloyds – Authorized Reinsurer (21%) Catlin Underwriting – Authorized Reinsurer (10%) Various Authorized and Unauthorized Reinsurers (69%) | \$100 million | \$50 million |

| Type of Contract | Reinsurer's Name | Company's Retention | Reinsurer's Maximum Limits |
|---|---|---------------------|----------------------------|
| <u>Workers' Compensation Terrorism XOL:</u> | | | |
| 1 st Excess of Loss | Tokio Millenium Reinsurance Ltd – Unauthorized Reinsurer (25%) Validus Reinsurance Ltd – Unauthorized Reinsurer (12%) Various Authorized and Unauthorized Reinsurers (13%) Company retains 50% of \$10 million | \$10 million | \$10 million |
| 2 nd Excess of Loss | Tokio Millenium Reinsurance Ltd – Unauthorized Reinsurer (25%) Validus Reinsurance Ltd - Unauthorized Reinsurer (12%) Various Authorized and Unauthorized Reinsurers (13%) Company retains 50% of \$30 million | \$20 million | \$30 million |
| 3 rd Excess of Loss | Tokio Millenium Reinsurance Ltd- Unauthorized Reinsurer (25%) Validus Reinsurance Ltd- Unauthorized Reinsurer (12%) Various Authorized and Unauthorized Reinsurers (13%) Company retains 50% of \$50 million | \$50 million | \$50 million |
| <u>Excess Workers' Compensation XOL:</u> | | | |
| 1 st Excess of Loss | Hannover Ruckversicherungs Aktiengesellschaft-Authorized Reinsurer (50%) Catlin Underwriting-Authorized Reinsurer (30%) Company retains 20% of \$2 million | \$250,000 | \$1.75 million |

| Type of Contract | Reinsurer's Name | Company's Retention | Reinsurer's Maximum Limits |
|--------------------------------|--|---------------------|----------------------------|
| 2 nd Excess of Loss | Hannover Ruckversicherungs Aktiengesellschaft-Authorized Reinsurer (35%) Brit-Lloyds Syndicate 2987- Authorized Reinsurer (20%) Paris Reinsurance-Unauthorized Reinsurer (20%) Various Authorized and Unauthorized Reinsurers (25%) | \$2 million | \$3 million |
| 3 rd Excess of Loss | Hannover Ruckversicherungs Aktiengesellschaft-Authorized Reinsurer (45%) Brit-Lloyds Syndicate 2987- Authorized Reinsurer (20%) Liberty-Lloyds Syndicate 4472- Authorized Reinsurer (15%) Various Authorized and Unauthorized Reinsurers (20%) | \$5 million | \$5 million |
| 4 th Excess of Loss | Hannover Ruckversicherungs Aktiengesellschaft-Authorized Reinsurer (15%) Brit-Lloyds Syndicate 2987- Authorized Reinsurer (20%) Liberty-Lloyds Syndicate 4472- Authorized Reinsurer (15%) Various Authorized and Unauthorized Reinsurers (50%) | \$10 million | \$10 million |
| 5 th Excess of Loss | Hannover Ruckversicherungs Aktiengesellschaft-Authorized Reinsurer (15%) Brit-Lloyds Syndicate 2987- Authorized Reinsurers (13%) Catlin Underwriting-Authorized Reinsurer (20%) Various Authorized and Unauthorized Reinsurers (52%) | \$20 million | \$30 million |

Retroactive Reinsurance

Effective April 1, 1998, the Company, and its wholly-owned subsidiary, Republic Insurance Company of California (RICC), entered into a retroactive reinsurance agreement with Converium, Ltd. (Converium).^{*} Under the terms of the agreement, the Company and RICC ceded 95% of \$60 million, in excess of \$390 million, of its loss and loss adjustment expense reserves to Converium.

The agreement pertains to workers' compensation losses unpaid as of March 31, 1998, for insured events with occurrence dates from January 1, 1988 through March 31, 1988. The total consideration paid by the Company and RICC for the agreement was \$14.7 million.

In accordance with the precepts of the Statement of Statutory Accounting Principles No. 62, the amount of retroactive reinsurance reserves ceded (\$18.1 million) is reported in the Company's 2008 Annual Statement as a contra-liability under the heading "Aggregate write-ins for liabilities," and the surplus gain resulting from retroactive reinsurance (\$18.1 million) is reflected as "Special surplus from retroactive reinsurance loss portfolio."

ACCOUNTS AND RECORDS

Information Systems Controls

A consulting firm contracted by the California Department of Insurance conducted a review of the Company's information system general controls. As referenced in the consultant's report, it is recommended that the Company formally document the annual review and update of its business continuity/disaster recovery plan.

*Effective September 17, 2007, Coverium, Ltd. changed its name to SCOR Holdings (Switzerland) Ltd.

FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of December 31, 2008

Underwriting and Investment Exhibit for the Year Ended December 31, 2008

Reconciliation of Surplus as Regards Policyholders
from December 31, 2004 through December 31, 2008

Statement of Financial Condition
as of December 31, 2008

| <u>Assets</u> | <u>Ledger and Nonledger Assets</u> | <u>Assets Not Admitted</u> | <u>Net Admitted Assets</u> | <u>Notes</u> |
|---|--|--------------------------------|--------------------------------|--------------|
| Bonds | \$746,643,793 | \$ | \$746,643,793 | |
| Preferred stocks | 1,556,600 | | 1,556,600 | |
| Common stocks | 23,846,891 | | 23,846,891 | |
| Cash and short-term investments | 23,968,878 | | 23,968,878 | |
| Investment income due or accrued | 7,436,606 | | 7,436,606 | |
| Uncollected premiums and agents' balances in course of collection | 11,065,165 | 610,977 | 10,454,188 | |
| Deferred premiums, agents' balances and installments booked but deferred and not yet due | 2,122,993 | 191,069 | 1,931,924 | |
| Accrued retrospective premiums | 48,751 | 4,875 | 43,876 | |
| Amounts recoverable from reinsurers | 13,469,590 | | 13,469,590 | |
| Funds held by or deposited with reinsured companies | 20,793 | | 20,793 | |
| Current federal and foreign income tax recoverable | 1,410,045 | | 1,410,045 | |
| Net deferred tax asset | 47,630,915 | 23,345,958 | 24,284,957 | |
| Guaranty funds receivable or on deposit | 69 | | 69 | |
| Electronic data processing equipment and software | 1,645,064 | 1,645,064 | | |
| Furniture and equipment | 445,212 | 445,212 | | |
| Aggregate write-ins for other than invested assets | <u>11,181,417</u> | <u>8,223,033</u> | <u>2,958,384</u> | |
| Total assets | <u>\$892,492,782</u> | <u>\$34,466,188</u> | <u>\$858,026,594</u> | |

Statement of Financial Condition
as of December 31, 2008
(Continued)

Liabilities, Surplus and Other Funds

| | | |
|--|----------------------|-----|
| Losses | \$460,653,603 | (1) |
| Loss adjustment expenses | 78,406,951 | (1) |
| Commissions payable, contingent commissions and other similar charges | 2,009,151 | |
| Other expenses | 9,103,206 | |
| Taxes, licenses and fees | (53,733) | |
| Unearned premiums | 27,042,101 | |
| Ceded reinsurance premiums payable | (8,231,583) | |
| Funds held by company under reinsurance treaties | 1,685,416 | |
| Amounts withheld or retained by company for account of others | 82,249 | |
| Provision for reinsurance | 3,691,515 | (2) |
| Payable to parent, subsidiaries and affiliates | 4,990,805 | |
| Payable for securities | 2,188,652 | |
| Aggregate write-ins for liabilities | <u>(16,412,887)</u> | |
| Total liabilities | 565,155,446 | |
| Aggregate write-ins for special surplus funds | \$ 18,082,432 | |
| Common capital stock | 3,500,000 | |
| Gross paid-in and contributed surplus | 179,097,968 | |
| Unassigned funds (surplus) | <u>92,190,748</u> | |
| Surplus as regards policyholders | <u>292,871,148</u> | |
| Total liabilities, surplus and other funds | <u>\$858,026,594</u> | |

Underwriting and Investment Exhibit
for the Year Ended December 31, 2008

Statement of Income

Underwriting Income

| | | |
|--------------------------------------|-------------------|--------------------|
| Premiums earned | | \$ 198,302,628 |
| Deductions: | | |
| Losses incurred | \$ 52,890,619 | |
| Loss expenses incurred | 40,321,930 | |
| Other underwriting expenses incurred | <u>69,007,090</u> | |
| Total underwriting deductions | | <u>162,219,639</u> |
| Net underwriting gain | | 36,082,989 |

Investment Income

| | | |
|------------------------------|--------------------|------------|
| Net investment income earned | \$ 38,371,067 | |
| Net realized capital losses | <u>(9,458,838)</u> | |
| Net investment gain | | 28,912,229 |

Other Income

| | | |
|---|--------------|----------------------|
| Net loss from agents' or premium balances charged off | \$ (293,382) | |
| Aggregate write-ins for miscellaneous income | <u>6,336</u> | |
| Total other income | | <u>(287,046)</u> |
| Net income before dividends to policyholders and before federal income taxes | | 64,708,172 |
| Dividends to policyholders | | 3,070,846 |
| Federal and income taxes incurred | | <u>19,842,127</u> |
| Net income | | <u>\$ 41,795,199</u> |

Capital and Surplus Account

| | | |
|---|-----------------|-----------------------|
| Surplus as regards policyholders, December 31, 2007 | | \$ 323,043,893 |
| Net income | \$ 41,795,199 | |
| Change in net unrealized capital losses | (551,161) | |
| Change in net deferred income tax | 1,679,708 | |
| Change in nonadmitted assets | (5,171,215) | |
| Change in provision for reinsurance | (2,949,922) | |
| Surplus adjustments – Paid in | 16,678,646 | |
| Dividends to stockholders | (81,600,000) | |
| Aggregate write-ins for losses in surplus | <u>(54,000)</u> | |
| Change in surplus as regards policyholders | | <u>(30,172,745)</u> |
| Surplus as regards policyholders, December 31, 2008 | | <u>\$ 292,871,148</u> |

Reconciliation of Surplus as Regards Policyholders
from December 31, 2004 through December 31, 2008

Surplus as regards policyholders, December 31, 2004
per Examination

\$242,555,602

| | <u>Gain in Surplus</u> | <u>Loss in Surplus</u> |
|--|----------------------------|----------------------------|
| Net income | \$251,900,594 | \$ |
| Change in net unrealized capital gains | 5,971,789 | |
| Change in net deferred income tax | | 2,506,506 |
| Change in nonadmitted assets and related items | | 2,316,076 |
| Change in provision for reinsurance | | 3,084,106 |
| Surplus adjustment – paid in | 69,666,852 | |
| Dividends to stockholders | | 291,600,000 |
| Aggregate write-ins for gains in surplus | <u>22,283,000</u> | |
| Totals | <u>\$349,822,235</u> | <u>\$299,506,688</u> |

Net increase in surplus as regards policyholders

50,315,547

Surplus as regards policyholders, December 31, 2008
per Examination

\$292,871,149

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Losses and Loss Adjustment Expenses

Based on the analysis by a Casualty Actuary from the California Department of Insurance, the Company's December 31, 2008 reserves for losses and loss adjustment expenses were determined to be reasonably stated.

(2) Provision for Reinsurance

For the purpose of establishing the provision for its overdue reinsurance reserve, the Company has historically maintained the practice of making separate calculations for its workers' compensation and excess liability lines of business by reinsurer. Calculation of the reserve on a composite line basis by reinsurer results in a reserve that is \$4.5 million greater than reported by the Company. With consideration given to the immateriality of the differential, no examination change was implemented. Management has indicated that beginning with the filing of the 3rd quarter 2009 statement, the Company will calculate the reserve strictly on a per reinsurer basis.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

Management and Control – Management Agreements (Page 5): The Company is hereby reminded that it must observe the requirements stipulated in California Insurance Code Section 1215.5(b)(4).

Accounts and Records – Information System Controls (Page 11): It is recommended that the Company formally document the annual review and update of its business continuity /disaster recovery plan.

Previous Report of Examination

Management and Control (Page 5): For the purpose of complying with California Insurance Code (CIC) Section 1215 (b)(4), it was recommended that the Company obtain approval for its executed workers' compensation handling agreement. Authorization for implementation of a replacement agreement was granted by the California Department of Insurance on August 14, 2007.

ACKNOWLEDGEMENT

The courtesy and cooperation extended by the Company's officers and employees during the course of this examination is hereby acknowledged.

Respectfully submitted,

/S/

David A. Fischman, CFE
Examiner-In-Charge
Senior Insurance Examiner
Department of Insurance
State of California